

CREDIT OPINION

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New Issue

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City of Albuquerque, New Mexico

New Issue: Moody's Assigns Aa1 to Albuquerque's, NM GO Bonds, Ser. 2017A; Outlook is Stable

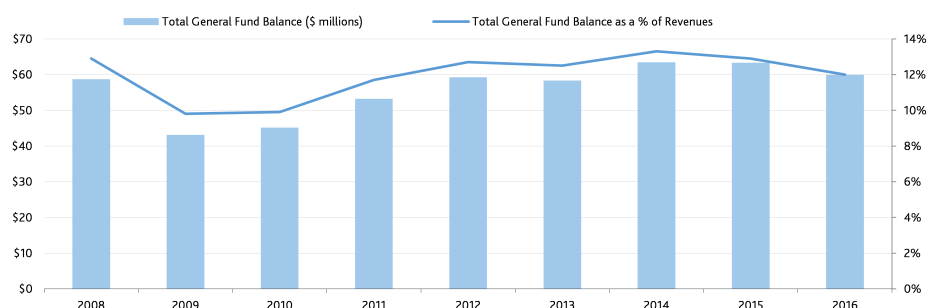
Summary Rating Rationale

Moody's Investors Service has assigned a Aa1 rating to the City of Albuquerque, NM's \$22.9 million General Obligation General Purpose Bonds, Series 2017A. Concurrently, Moody's has affirmed the Aa1 rating on the city's outstanding rated parity debt. The outlook remains stable.

The Aa1 rating reflects the city's sizeable tax base that serves as a regional economic hub for the state; favorable debt profile with rapid principal amortization; and, average wealth indices. The rating further incorporates the city's narrow, albeit stable, financial position and elevated pension burden.

Exhibit 1

Reserves are Stable Overall; City Manages to Operate within Narrow Margins



Source: City's CAFRs; Moody's Investors Service

Credit Strengths

- » Large and diverse tax base that serves as the economic engine for the state of New Mexico
- » Favorable debt profile with rapid principal amortization

Credit Challenges

- » Tepid economic recovery; reliance on economically sensitive gross receipts tax (GRT) revenues
- » Limited financial position in comparison to similarly rated entities
- » Phase out of hold harmless distributions beginning fiscal 2016

- » Increased public safety expenditures after Department of Justice settlement
- » Steadily increasing pension burden

Rating Outlook

The stable outlook reflects the ongoing recovery and overall stabilization of the city's economy. This trend is expected to remain slow, but positive, over the near-term. The outlook further incorporates the expectation that financial reserves will remain stable, if narrow, in the future, supported by conservative budgeting and formal fund balance policies. Future rating actions will assess the city's economic stability and ability to maintain structural balance, especially in light of an increasing pension burden.

Factors that Could Lead to an Upgrade

- » Trend of operating surpluses increasing reserves
- » Significant economic expansion and diversification

Factors that Could Lead to a Downgrade

- » Trend of imbalanced operations resulting in deterioration of financial reserves
- » Tax base contraction or economic stagnation; declines in GRT collections
- » Further increases in the city's pension burden, tread water gap or fixed cost burden

Key Indicators

Exhibit 2

Albuquerque (City of) NM	2011	2012	2013	2014	2015
Economy/Tax Base					
Total Full Value (\$000)	\$ 35,797,196	\$ 35,890,180	\$ 35,664,833	\$ 35,937,076	\$ 36,722,507
Full Value Per Capita	\$ 66,414	\$ 65,844	\$ 64,867	\$ 64,918	\$ 66,337
Median Family Income (% of US Median)	93.9%	93.1%	93.0%	92.1%	92.1%
Finances					
Operating Revenue (\$000)	\$ 504,992	\$ 526,417	\$ 530,879	\$ 535,395	\$ 549,905
Fund Balance as a % of Revenues	14.6%	14.9%	13.5%	13.0%	14.3%
Cash Balance as a % of Revenues	23.3%	22.5%	23.2%	24.7%	25.3%
Debt/Pensions					
Net Direct Debt (\$000)	\$ 441,365	\$ 353,229	\$ 412,111	\$ 414,339	\$ 624,828
Net Direct Debt / Operating Revenues (x)	0.9x	0.7x	0.8x	0.8x	1.1x
Net Direct Debt / Full Value (%)	1.2%	1.0%	1.2%	1.2%	1.7%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	N/A	2.7x	2.8x	2.7x	2.3x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	N/A	3.9%	4.2%	4.1%	3.5%

Source: City's CAFRs; Moody's Investors Service

Detailed Rating Considerations

Economy and Tax Base: Large Tax Base with Regional Economic Importance

The city's economy and tax base will remain stable and sizeable over the mid-term given regional importance and institutional presence. Located in north central New Mexico (Aa1 negative), the City of Albuquerque is home to approximately 25% of the state's population. After experiencing modest assessed value declines in fiscal 2011 and 2013 correlated with the most recent economic

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recession, the city's tax base returned to slow, but positive, expansion from fiscal 2014 to 2017. The five year average growth rate of 1.4% annually further highlights the slow economic recovery. Fiscal 2017 assessed values increased by 3.2% over the prior year to reach \$12.8 billion, derived from a large \$38.5 billion full valuation. Management anticipates the tax base will remain stable in the near future. Major ongoing development includes expansion of existing businesses, such as healthcare clinics and call centers; construction of national chains; and, investment in the city's downtown (InnovateABQ).

The December 2016 Moody's Economy.com Albuquerque report indicates that the economy is in recovery. Despite slowdown in manufacturing, driven by layoffs at the Intel plant, and retail, the public sector presence continues to provide a stabilizing influence. The report notes that shortage of high-skilled professional jobs, that are not related to federal contracts, will keep household income growth lagging that of the US.

Major employers in the Albuquerque MSA include the University of New Mexico, Kirtland Air Force Base (AFB), and Sandia National Laboratories. The institutional presence provided by these entities is an anchor for the local economy. Healthcare and high-tech industries also have significant presence in the employment base. The city's December 2016 unemployment rate of 5.2% was below the state (6.3%) but above the nation (4.5%) for the same time-period. Resident wealth levels are average with per capita income and median family income (2014 American Community Survey) approximating 94.1% and 92.1% of national levels, respectively.

Financial Operations and Reserves: Stable Overall, but Narrow for the Rating Category

Since fiscal 2010, the city has made a concentrated effort to balance operations through expenditure cuts and property tax increases. Management's efforts were largely successful with surpluses reported in fiscal 2010, 2011, 2012 and 2014. Fiscal 2015 ended with a modest deficit of \$135,000, reducing General Fund balance to \$63.3 million, or 12.9% of revenues. By statute, the city is required to maintain a minimum General Fund balance of 1/12th (8.3%) of budgeted expenditures, and officials are focused on increasing that floor to 1/10th (10%) over the next several fiscal years.

Fiscal 2016 ended with a deficit of \$3.4 million for an ending General Fund balance of \$60 million, or 12% of revenues. Revenues, which did increase by 2.1% year-over-year, were outpaced by expenditures, particularly another increase of \$4.4 million for public safety, a consequence of the settlement with the US Department of Justice related to use of excessive force. The cost of reform is incorporated in the police department's budget to the tune of around \$4 million per year through fiscal 2020, tapering slightly thereafter. Liabilities related to claims and judgments associated with police actions are reported in the Risk Management Fund, a separate fund used to account for the cost of tort and other claims insurance coverage. In fiscal 2016, the fund reported \$68.6 million remaining in long-term claims and judgments, resulting in a negative net asset position of \$39.7 million. Management plans to return the fund to structural balance by fiscal 2025 through increased charges to departments.

The fiscal 2017 budget assumed revenues of \$515.4 million, and expenditures of \$526.4 million, including \$13.5 million in non-recurring costs (capital outlay). Based on performance through January 2017, estimated actuals were adjusted to revenues of \$512.9 million and expenditures of \$528.9 million, including \$17 million in one-time costs. The city has historically performed better than projected, and management stresses that these figures are conservative. Officials explain that they plan to close the gap through a freeze on discretionary expenses, as well as delays in hiring.

Moody's notes the city is fairly reliant on economically sensitive revenues (GRT), which represent approximately 65% of the operating budget. The hold harmless phase out began in fiscal 2016, and will run through fiscal 2030. GRT collections will decrease by approximately \$2.2 million to \$2.6 million annually, compounding to around \$12 million reduction by 2020. The phase out will effectively mute revenue growth over the mid-term. Due to the strength of the local economy, officials do believe that GRT revenues will continue increasing annually by 2% to 4%, net of the phase out. Additionally, city officials could impose up to 3/8th of a hold harmless gross receipts tax without voter approval, which would generate an additional \$51 million on an annual basis. There are no plans at this time to implement new taxes.

The city's five-year forecast is conservative, with management incorporating current trends, department requests and inflationary factors into their expenditure projections. The end result is operating deficits through fiscal 2021. The city does face challenges: in addition to GRT growth being tempered by the hold harmless phase out, officials report that turnover has lessened, reducing vacancy savings, and that departments are staffed as efficiently as possible, hindering ability to make cuts. New operating costs for Albuquerque Rapid Transit, zoo exhibits and streets are coming online to the tune of \$7.3 million to \$11.5 million per year. However, to balance

the budget on a yearly basis, management will consider delaying opening dates of projects, deferring maintenance, eliminating pay increases or reducing contractual obligations. Future reviews will focus on the city's ability to maintain balanced, if not surplus, operations. Management has shown an ability to operate within narrow margins; however, the city's reserve of 8.3% is weak for the rating category, and reserves at least equal to this policy is key to maintenance of the Aa1.

LIQUIDITY

General Fund cash reserves are slightly below total General Fund balance, but in line with historic levels. At fiscal 2015 year-end, the city reported \$56.6 million in General Fund cash, or 11.6% of revenues. With the use of reserves in fiscal 2016, cash declined to \$53.5 million, or 10.7% of revenues.

Debt and Pensions: Manageable Debt Burden Benefitting from Rapid Principal Payout; Elevated Pension Burden

Despite plans for additional borrowing over the mid-term, the city's debt burden will likely remain manageable given rapid principal retirement. Inclusive of the current sale, the general obligation debt burden is modest at 1.1% of fiscal 2017 full value, increasing to 1.8% of fiscal 2017 full value when GRT debt (Moody's rated Aa2) is included. By statute, the city's debt burden is capped at 4% of assessed valuation, or, in fiscal 2017, \$512.4 million. As of January 2017, the city has utilized 67% of available bonding capacity. Series 2017A will exhaust the remaining authorization from the November 2015 election. Officials plan to approach voters again in 2017 with a \$121.5 million bond package.

DEBT STRUCTURE

Principal amortization is rapid with 95.3% of outstanding debt (inclusive of current issuances) is retired in ten years. All long-term general obligation debt matures in 2030. The city's debt policy only allows the issuance of bonds with 13-year maturities or less.

DEBT-RELATED DERIVATIVES

The city has no exposure to variable rate debt or interest rate swaps.

PENSIONS AND OPEB

The city has an above-average employee pension burden, based on unfunded liabilities for its share of the Public Employees Retirement Association (PERA), a cost sharing plan administered by the state. Albuquerque's annual contributions into the plan have been at the statutorily required amount, which is well below the actuarially required amounts and has driven the large unfunded liability. Moody's fiscal 2016 adjusted net pension liability (ANPL) for the city, under our methodology for adjusting reported pension data, is \$1.6 billion, or an above average 2.82 times operating revenues. The three-year average of the city's ANPL to operating revenues is 2.43 times, while the three-year average of ANPL to full value is a high 3.66%.

The city's ANPL has increased annually since fiscal 2014. In fiscal 2016, pension contributions of \$33.3 million were below Moody's "tread water" value of \$53.6 million, a credit negative. The "tread water" indicator measures the annual contributions required to prevent the reported net pension liability from increasing, under reported assumptions. The city's fixed costs, including debt service, pension and OPEB contributions, are approximately 22% of operating revenues, which is somewhat elevated, but still in-line with similarly rated credits. However, if the city's contributions are replaced with tread water, the fixed cost burden increases to 25.8%. Continued underfunding of the pension could result in downward rating pressure.

Moody's ANPL reflects certain adjustments we make to improve comparability of reported pension liabilities. The adjustments are not intended to replace the city's reported liability information, but to improve comparability with other rated entities. For more information on Moody's insights on employee pensions and the related credit impact on companies, government, and other entities across the globe, please visit Moody's on Pensions at www.moody.com/pensions.

Management and Governance

New Mexico cities have an institutional framework score of "A," or moderate. Cities receive the majority of their revenues through gross receipt and property taxes, which in combination are moderately predictable. Most cities are at the O&M property tax levy cap but have a moderate ability to raise revenues. Expenditures are moderately predictable and mainly consist of salaries and public safety. Cities have a moderate ability to reduce expenditures due to high fixed costs.

The City is a home rule municipality, with its charter originally adopted in 1971, and has a Mayor-Council form of government with a salaried full-time Mayor elected every four years.

Legal Security

The bonds are secured by a direct and continuing property tax levied, without limitation as to rate of amount, on all taxable property within the city.

Use of Proceeds

Proceeds from the Series 2017A bonds will be used for various capital projects, including public safety, community enhancement, energy conservation, library and streets.

Obligor Profile

Albuquerque is the largest city in the State of New Mexico (GO rated Aa1 negative), accounting for roughly one-quarter of the State's population. Located at the center of the State in Bernalillo County (Aaa stable) at the intersection of two major interstate highways and served by both rail and air, Albuquerque is the major trade, commercial and financial center of the State.

Methodology

The principal methodology used in this rating was US Local Government General Obligation Debt published in December 2016. Please see the Rating Methodologies page on www.moody.com for a copy of this methodology.

Ratings

Exhibit 3

Albuquerque (City of) NM

Issue	Rating
General Obligation General Purpose Bonds, Series 2017A	Aa1
Rating Type	Underlying LT
Sale Amount	\$22,900,000
Expected Sale Date	03/06/2017
Rating Description	General Obligation

Source: Moody's Investors Service

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